

However, if an issuer enters into an arrangement for private business use a substantial period before the right to actual private business use commences and the arrangement transfers ownership or is an arrangement for other long-term use (such as a lease for a significant portion of the remaining economic life of financed property), private business use commences on the date the arrangement is entered into, even if the right to actual use commences after the measurement period. For this purpose, 10 percent of the measurement period is generally treated as a substantial period.

(8) *Examples.* The following examples illustrate the application of this paragraph (g):

Example 1. Research facility. University U, a state owned and operated university, owns and operates a research facility. U proposes to finance general improvements to the facility with the proceeds of an issue of bonds. U enters into sponsored research agreements with nongovernmental persons that result in private business use because the sponsors will own title to any patents resulting from the research. The governmental research conducted by U and the research U conducts for the sponsors take place simultaneously in all laboratories within the research facility. All laboratory equipment is available continuously for use by workers who perform both types of research. Because it is not possible to predict which research projects will be successful, it is not reasonably practicable to estimate the relative revenues expected to result from the governmental and nongovernmental research. U contributed 90 percent of the cost of the facility and the nongovernmental persons contributed 10 percent of the cost. Under this section, the nongovernmental persons are using the facility for a private business use on the same basis as the government use of the facility. The portions of the costs contributed by the various users of the facility provide a reasonable basis that properly reflects the proportionate benefit to be derived by the users of the facility. The nongovernmental persons are treated as using 10 percent of the proceeds of the issue.

Example 2. Stadium. (i) City L issues bonds and uses all of the proceeds to construct a stadium. L enters into a long-term contract with a professional sports team T under which T will use the stadium 20 times during each year. These uses will occur on nights and weekends. L reasonably expects that the stadium will be used more than 180 other times each year, none of which will give rise to private business use. This expectation is based on a feasibility study and historical

use of the old stadium that is being replaced by the new stadium. There is no significant difference in the value of T's uses when compared to the other uses of the stadium, taking into account the payments that T is reasonably expected to make for its use. Assuming no other private business use, the issue does not meet the private business use test because not more than 10 percent of the use of the facility is for a private business use.

(ii) The facts are the same as in *Example 2(i)*, except that L reasonably expects that the stadium will be used not more than 60 other times each year, none of which will give rise to private business use. The issue meets the private business use test because 25 percent of the proceeds are used for a private business use.

Example 3. Airport terminal areas treated as common areas. City N issues bonds to finance the construction of an airport terminal. Eighty percent of the leasable space of the terminal will be leased to private air carriers. The remaining 20 percent of the leasable space will be used for the term of the bonds by N for its administrative purposes. The common areas of the terminal, including waiting areas, lobbies, and hallways are treated as 80 percent used by the air carriers for purposes of the private business use test.

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§ 1.141-4 Private security or payment test.

(a) *General rule—(1) Private security or payment.* The private security or payment test relates to the nature of the security for, and the source of, the payment of debt service on an issue. The private payment portion of the test takes into account the payment of the debt service on the issue that is directly or indirectly to be derived from payments (whether or not to the issuer or any related party) in respect of property, or borrowed money, used or to be used for a private business use. The private security portion of the test takes into account the payment of the debt service on the issue that is directly or indirectly secured by any interest in property used or to be used for a private business use or payments in respect of property used or to be used for a private business use. For additional rules for output facilities, see § 1.141-7.

(2) *Aggregation of private payments and security.* For purposes of the private security or payment test, payments

taken into account as private payments and payments or property taken into account as private security are aggregated. However, the same payments are not taken into account as both private security and private payments.

(3) *Underlying arrangement.* The security for, and payment of debt service on, an issue is determined from both the terms of the bond documents and on the basis of any underlying arrangement. An underlying arrangement may result from separate agreements between the parties or may be determined on the basis of all of the facts and circumstances surrounding the issuance of the bonds. For example, if the payment of debt service on an issue is secured by both a pledge of the full faith and credit of a state or local governmental unit and any interest in property used or to be used in a private business use, the issue meets the private security or payment test.

(b) *Measurement of private payments and security*—(1) *Scope.* This paragraph (b) contains rules that apply to both private security and private payments.

(2) *Present value measurement*—(i) *Use of present value.* In determining whether an issue meets the private security or payment test, the present value of the payments or property taken into account is compared to the present value of the debt service to be paid over the term of the issue.

(ii) *Debt service*—(A) *Debt service paid from proceeds.* Debt service does not include any amount paid or to be paid from sale proceeds or investment proceeds. For example, debt service does not include payments of capitalized interest funded with proceeds.

(B) *Adjustments to debt service.* Debt service is adjusted to take into account payments and receipts that adjust the yield on an issue for purposes of section 148(f). For example, debt service includes fees paid for qualified guarantees under § 1.148-4(f) and is adjusted to take into account payments and receipts on qualified hedges under § 1.148-4(h).

(iii) *Computation of present value*—(A) *In general.* Present values are determined by using the yield on the issue as the discount rate and by discounting all amounts to the issue date. See,

however, § 1.141-13 for special rules for refunding bonds.

(B) *Fixed yield issues.* For a fixed yield issue, yield is determined on the issue date and is not adjusted to take into account subsequent events.

(C) *Variable yield issues.* The yield on a variable yield issue is determined over the term of the issue. To determine the reasonably expected yield as of any date, the issuer may assume that the future interest rate on a variable yield bond will be the then-current interest rate on the bonds determined under the formula prescribed in the bond documents. A deliberate action requires a recomputation of the yield on the variable yield issue to determine the present value of payments under that arrangement. In that case, the issuer must use the yield determined as of the date of the deliberate action for purposes of determining the present value of payments under the arrangement causing the deliberate action. See paragraph (g) of this section, *Example 3*.

(iv) *Application to private security.* For purposes of determining the present value of debt service that is secured by property, the property is valued at fair market value as of the first date on which the property secures bonds of the issue.

(c) *Private payments*—(1) *In general.* This paragraph (c) contains rules that apply to private payments.

(2) *Payments taken into account*—(i) *Payments for use*—(A) *In general.* Both direct and indirect payments made by any nongovernmental person that is treated as using proceeds of the issue are taken into account as private payments to the extent allocable to the proceeds used by that person. Payments are taken into account as private payments only to the extent that they are made for the period of time that proceeds are used for a private business use. Payments for a use of proceeds include payments (whether or not to the issuer) in respect of property financed (directly or indirectly) with those proceeds, even if not made by a private business user. Payments are not made in respect of financed property if those payments are directly allocable to other property being directly used by the person making the

payment and those payments represent fair market value compensation for that other use. See paragraph (g) of this section, *Example 4* and *Example 5*. See also paragraph (c)(3) of this section for rules relating to allocation of payments to the source or sources of funding of property.

(B) *Payments not to exceed use.* Payments with respect to proceeds that are used for a private business use are not taken into account to the extent that the present value of those payments exceeds the present value of debt service on those proceeds. Payments need not be directly derived from a private business user, however, to be taken into account. Thus, if 7 percent of the proceeds of an issue is used by a person over the measurement period, payments with respect to the property financed with those proceeds are taken into account as private payments only to the extent that the present value of those payments does not exceed the present value of 7 percent of the debt service on the issue.

(C) *Payments for operating expenses.* Payments by a person for a use of proceeds do not include the portion of any payment that is properly allocable to the payment of ordinary and necessary expenses (as defined under section 162) directly attributable to the operation and maintenance of the financed property used by that person. For this purpose, general overhead and administrative expenses are not directly attributable to those operations and maintenance. For example, if an issuer receives \$5,000 rent during the year for use of space in a financed facility and during the year pays \$500 for ordinary and necessary expenses properly allocable to the operation and maintenance of that space and \$400 for general overhead and general administrative expenses properly allocable to that space, \$500 of the \$5,000 received would not be considered a payment for the use of the proceeds allocable to that space (regardless of the manner in which that \$500 is actually used).

(ii) *Refinanced debt service.* Payments of debt service on an issue to be made from proceeds of a refunding issue are taken into account as private payments in the same proportion that the present value of the payments taken

into account as private payments for the refunding issue bears to the present value of the debt service to be paid on the refunding issue. For example, if all the debt service on a note is paid with proceeds of a refunding issue, the note meets the private security or payment test if (and to the same extent that) the refunding issue meets the private security or payment test. This paragraph (c)(2)(ii) does not apply to payments that arise from deliberate actions that occur more than 3 years after the retirement of the prior issue that are not reasonably expected on the issue date of the refunding issue. For purposes of this paragraph (c)(2)(ii), whether an issue is a refunding issue is determined without regard to § 1.150-1(d)(2)(i) (relating to certain payments of interest).

(3) *Allocation of payments*—(i) *In general.* Private payments for the use of property are allocated to the source or different sources of funding of property. The allocation to the source or different sources of funding is based on all of the facts and circumstances, including whether an allocation is consistent with the purposes of section 141. In general, a private payment for the use of property is allocated to a source of funding based upon the nexus between the payment and both the financed property and the source of funding. For this purpose, different sources of funding may include different tax-exempt issues, taxable issues, and amounts that are not derived from a borrowing, such as revenues of an issuer (equity).

(ii) *Payments for use of discrete property.* Payments for the use of a discrete facility (or a discrete portion of a facility) are allocated to the source or different sources of funding of that discrete property.

(iii) *Allocations among two or more sources of funding.* In general, except as provided in paragraphs (c)(3)(iv) and (v) of this section, if a payment is made for the use of property financed with two or more sources of funding (for example, equity and a tax-exempt issue), that payment must be allocated to those sources of funding in a manner that reasonably corresponds to the relative amounts of those sources of funding that are expended on that property.

If an issuer has not retained records of amounts expended on the property (for example, records of costs of a building that was built 30 years before the allocation), an issuer may use reasonable estimates of those expenditures. For this purpose, costs of issuance and other similar neutral costs are allocated ratably among expenditures in the same manner as in § 1.141-3(g)(6). A payment for the use of property may be allocated to two or more issues that finance property according to the relative amounts of debt service (both paid and accrued) on the issues during the annual period for which the payment is made, if that allocation reasonably reflects the economic substance of the arrangement. In general, allocations of payments according to relative debt service reasonably reflect the economic substance of the arrangement if the maturity of the bonds reasonably corresponds to the reasonably expected economic life of the property and debt service payments on the bonds are approximately level from year to year.

(iv) *Payments made under an arrangement entered into in connection with issuance of bonds.* A private payment for the use of property made under an arrangement that is entered into in connection with the issuance of the issue that finances that property generally is allocated to that issue. Whether an arrangement is entered into in connection with the issuance of an issue is determined on the basis of all of the facts and circumstances. An arrangement is ordinarily treated as entered into in connection with the issuance of an issue if—

(A) The issuer enters into the arrangement during the 3-year period beginning 18 months before the issue date; and

(B) The amount of payments reflects all or a portion of debt service on the issue.

(v) *Allocations to equity.* A private payment for the use of property may be allocated to equity before payments are allocated to an issue only if—

(A) Not later than 60 days after the date of the expenditure of those amounts, the issuer adopts an official intent (in a manner comparable to § 1.150-2(e)) indicating that the issuer

reasonably expects to be repaid for the expenditure from a specific arrangement; and

(B) The private payment is made not later than 18 months after the later of the date the expenditure is made or the date the project is placed in service.

(d) *Private security*—(1) *In general.* This paragraph (d) contains rules that relate to private security.

(2) *Security taken into account.* The property that is the security for, or the source of, the payment of debt service on an issue need not be property financed with proceeds. For example, unimproved land or investment securities used, directly or indirectly, in a private business use that secures an issue provides private security. Private security (other than financed property and private payments) for an issue is taken into account under section 141(b), however, only to the extent it is provided, directly or indirectly, by a user of proceeds of the issue.

(3) *Pledge of unexpended proceeds.* Proceeds qualifying for an initial temporary period under § 1.148-2(e)(2) or (3) or deposited in a reasonably required reserve or replacement fund (as defined in § 1.148-2(f)(2)(i)) are not taken into account under this paragraph (d) before the date on which those amounts are either expended or loaned by the issuer to an unrelated party.

(4) *Secured by any interest in property or payments.* Property used or to be used for a private business use and payments in respect of that property are treated as private security if any interest in that property or payments secures the payment of debt service on the bonds. For this purpose, the phrase any interest in is to be interpreted broadly and includes, for example, any right, claim, title, or legal share in property or payments.

(5) *Payments in respect of property.* The payments taken into account as private security are payments in respect of property used or to be used for a private business use. Except as otherwise provided in this paragraph (d)(5) and paragraph (d)(6) of this section, the rules in paragraphs (c)(2)(i)(A) and (B) and (c)(2)(ii) of this section apply to determine the amount of payments treated as payments in respect of property

used or to be used for a private business use. Thus, payments made by members of the general public for use of a facility used for a private business use (for example, a facility that is the subject of a management contract that results in private business use) are taken into account as private security to the extent that they are made for the period of time that property is used by a private business user.

(6) *Allocation of security among issues.* In general, property or payments from the disposition of that property that are taken into account as private security are allocated to each issue secured by the property or payments on a reasonable basis that takes into account bondholders' rights to the payments or property upon default.

(e) *Generally applicable taxes*—(1) *General rule.* For purposes of the private security or payment test, generally applicable taxes are not taken into account (that is, are not payments from a nongovernmental person and are not payments in respect of property used for a private business use).

(2) *Definition of generally applicable taxes.* A generally applicable tax is an enforced contribution exacted pursuant to legislative authority in the exercise of the taxing power that is imposed and collected for the purpose of raising revenue to be used for governmental or public purposes. A generally applicable tax must have a uniform tax rate that is applied to all persons of the same classification in the appropriate jurisdiction and a generally applicable manner of determination and collection.

(3) *Special charges.* A special charge (as defined in this paragraph (e)(3)) is not a generally applicable tax. For this purpose, a special charge means a payment for a special privilege granted or regulatory function (for example, a license fee), a service rendered (for example, a sanitation services fee), a use of property (for example, rent), or a payment in the nature of a special assessment to finance capital improvements that is imposed on a limited class of persons based on benefits received from the capital improvements financed with the assessment. Thus, a special assessment to finance infrastructure improvements in a new industrial park (such as sidewalks,

streets, streetlights, and utility infrastructure improvements) that is imposed on a limited class of persons composed of property owners within the industrial park who benefit from those improvements is a special charge. By contrast, an otherwise qualified generally applicable tax (such as a generally applicable ad valorem tax on all real property within a governmental taxing jurisdiction) or an eligible PILOT under paragraph (e)(5) of this section that is based on such a generally applicable tax is not treated as a special charge merely because the taxes or PILOTs received are used for governmental or public purposes in a manner which benefits particular property owners.

(4) *Manner of determination and collection*—(i) *In general.* A tax does not have a generally applicable manner of determination and collection to the extent that one or more taxpayers make any impermissible agreements relating to payment of those taxes. An impermissible agreement relating to the payment of a tax is taken into account whether or not it is reasonably expected to result in any payments that would not otherwise have been made. For example, if an issuer uses proceeds to make a grant to a taxpayer to improve property, agreements that impose reasonable conditions on the use of the grant do not cause a tax on that property to fail to be a generally applicable tax. If an agreement by a taxpayer causes the tax imposed on that taxpayer not to be treated as a generally applicable tax, the entire tax paid by that taxpayer is treated as a special charge, unless the agreement is limited to a specific portion of the tax.

(ii) *Impermissible agreements.* The following are examples of agreements that cause a tax to fail to have a generally applicable manner of determination and collection: an agreement to be personally liable on a tax that does not generally impose personal liability, to provide additional credit support such as a third party guarantee, or to pay unanticipated shortfalls; an agreement regarding the minimum market value of property subject to property tax; and an agreement not to challenge or seek deferral of the tax.

(iii) *Permissible agreements.* The following are examples of agreements that do not cause a tax to fail to have a generally applicable manner of determination and collection: an agreement to use a grant for specified purposes (whether or not that agreement is secured); a representation regarding the expected value of the property following the improvement; an agreement to insure the property and, if damaged, to restore the property; a right of a grantor to rescind the grant if property taxes are not paid; and an agreement to reduce or limit the amount of taxes collected to further a bona fide governmental purpose. For example, an agreement to abate taxes to encourage a property owner to rehabilitate property in a distressed area is a permissible agreement.

(5) *Payments in lieu of taxes.* A tax equivalency payment or other payment in lieu of a tax ("PILOT") is treated as a generally applicable tax if it meets the requirements of paragraphs (e)(5)(i) through (iv) of this section—

(i) *Maximum amount limited by underlying generally applicable tax.* The PILOT is not greater than the amount imposed by a statute for a generally applicable tax in each year.

(ii) *Commensurate with a generally applicable tax.* The PILOT is commensurate with the amount imposed by a statute for a generally applicable tax in each year under the commensurate standard set forth in this paragraph (e)(5)(ii). For this purpose, except as otherwise provided in this paragraph (e)(5)(ii), a PILOT is commensurate with a generally applicable tax only if it is equal to a fixed percentage of the generally applicable tax that would otherwise apply in each year or it reflects a fixed adjustment to the generally applicable tax that would otherwise apply in each year. A PILOT based on a property tax does not fail to be commensurate with the property tax as a result of changes in the level of the percentage of or adjustment to that property tax for a reasonable phase-in period ending when the subject property is placed in service (as defined in § 1.150-2(c)). A PILOT based on a property tax must take into account the current assessed value of the property for property tax purposes for each year

in which the PILOT is paid and that assessed value must be determined in the same manner and with the same frequency as property subject to the property tax. A PILOT is not commensurate with a generally applicable tax, however, if the PILOT is set at a fixed dollar amount (for example, fixed debt service on a bond issue) that cannot vary with changes in the level of the generally applicable tax on which it is based.

(iii) *Use of PILOTs for governmental or public purposes.* The PILOT is to be used for governmental or public purposes for which the generally applicable tax on which it is based may be used.

(iv) *No special charges.* The PILOT is not a special charge under paragraph (e)(3) of this section.

(f) *Certain waste remediation bonds—(1) Scope.* This paragraph (f) applies to bonds issued to finance hazardous waste clean-up activities on privately owned land (hazardous waste remediation bonds).

(2) *Persons that are not private users.* Payments from nongovernmental persons who are not (other than coincidentally) either users of the site being remediated or persons potentially responsible for disposing of hazardous waste on that site are not taken into account as private security. This paragraph (f)(2) applies to payments that secure (directly or indirectly) the payment of principal of, or interest on, the bonds under the terms of the bonds. This paragraph (f)(2) applies only if the payments are made pursuant to either a generally applicable state or local taxing statute or a state or local statute that regulates or restrains activities on an industry-wide basis of persons who are engaged in generating or handling hazardous waste, or in refining, producing, or transporting petroleum, provided that those payments do not represent, in substance, payment for the use of proceeds. For this purpose, a state or local statute that imposes payments that have substantially the same character as those described in Chapter 38 of the Code are treated as generally applicable taxes.

(3) *Persons that are private users.* If payments from nongovernmental persons who are either users of the site

being remediated or persons potentially responsible for disposing of hazardous waste on that site do not secure (directly or indirectly) the payment of principal of, or interest on, the bonds under the terms of the bonds, the payments are not taken into account as private payments. This paragraph (f)(3) applies only if at the time the bonds are issued the payments from those nongovernmental persons are not material to the security for the bonds. For this purpose, payments are not material to the security for the bonds if—

(i) The payments are not required for the payment of debt service on the bonds;

(ii) The amount and timing of the payments are not structured or designed to reflect the payment of debt service on the bonds;

(iii) The receipt or the amount of the payment is uncertain (for example, as of the issue date, no final judgment has been entered into against the nongovernmental person);

(iv) The payments from those nongovernmental persons, when and if received, are used either to redeem bonds of the issuer or to pay for costs of any hazardous waste remediation project; and

(v) In the case when a judgment (but not a final judgment) has been entered by the issue date against a nongovernmental person, there are, as of the issue date, costs of hazardous waste remediation other than those financed with the bonds that may be financed with the payments.

(g) *Examples.* The following examples illustrate the application of this section:

Example 1. Aggregation of payments. State B issues bonds with proceeds of \$10 million. B uses \$9.7 million of the proceeds to construct a 10-story office building. B uses the remaining \$300,000 of proceeds to make a loan to Corporation Y. In addition, Corporation X leases 1 floor of the building for the term of the bonds. Under all of the facts and circumstances, it is reasonable to allocate 10 percent of the proceeds to that 1 floor. As a percentage of the present value of the debt service on the bonds, the present value of Y's loan repayments is 3 percent and the present value of X's lease payments is 8 percent. The bonds meet the private security or payment test because the private payments taken into account are more than 10 percent of the

present value of the debt service on the bonds.

Example 2. Indirect private payments. J, a political subdivision of a state, will issue several series of bonds from time to time and will use the proceeds to rehabilitate urban areas. Under all of the facts and circumstances, the private business use test will be met with respect to each issue that will be used for the rehabilitation and construction of buildings that will be leased or sold to nongovernmental persons for use in their trades or businesses. Nongovernmental persons will make payments for these sales and leases. There is no limitation either on the number of issues or the aggregate amount of bonds that may be outstanding. No group of bondholders has any legal claim prior to any other bondholders or creditors with respect to specific revenues of J, and there is no arrangement whereby revenues from a particular project are paid into a trust or constructive trust, or sinking fund, or are otherwise segregated or restricted for the benefit of any group of bondholders. There is, however, an unconditional obligation by J to pay the principal of, and the interest on, each issue. Although not directly pledged under the terms of the bond documents, the leases and sales are underlying arrangements. The payments relating to these leases and sales are taken into account as private payments to determine whether each issue of bonds meets the private security or payment test.

Example 3. Computation of payment in variable yield issues. (i) City M issues general obligation bonds with proceeds of \$10 million to finance a 5-story office building. The bonds bear interest at a variable rate that is recomputed monthly according to an index that reflects current market yields. The yield that the interest index would produce on the issue date is 6 percent. M leases 1 floor of the office building to Corporation T, a nongovernmental person, for the term of the bonds. Under all of the facts and circumstances, T is treated as using more than 10 percent of the proceeds. Using the 6 percent yield as the discount rate, M reasonably expects on the issue date that the present value of lease payments to be made by T will be 8 percent of the present value of the total debt service on the bonds. After the issue date of the bonds, interest rates decline significantly, so that the yield on the bonds over their entire term is 4 percent. Using this actual 4 percent yield as the discount rate, the present value of lease payments made by T is 12 percent of the present value of the actual total debt service on the bonds. The bonds are not private activity bonds because M reasonably expected on the issue date that the bonds would not meet the private security or payment test and because M

did not take any subsequent deliberate action to meet the private security or payment test.

(ii) The facts are the same as *Example 3(i)*, except that 5 years after the issue date M leases a second floor to Corporation S, a nongovernmental person, under a long-term lease. Because M has taken a deliberate action, the present value of the lease payments must be computed. On the date this lease is entered into, M reasonably expects that the yield on the bonds over their entire term will be 5.5 percent, based on actual interest rates to date and the then-current rate on the variable yield bonds. M uses this 5.5 percent yield as the discount rate. Using this 5.5 percent yield as the discount rate, as a percentage of the present value of the debt service on the bonds, the present value of the lease payments made by S is 3 percent. The bonds are private activity bonds because the present value of the aggregate private payments is greater than 10 percent of the present value of debt service.

Example 4. Payments not in respect of financed property. In order to further public safety, City Y issues tax assessment bonds the proceeds of which are used to move existing electric utility lines underground. Although the utility lines are owned by a nongovernmental utility company, that company is under no obligation to move the lines. The debt service on the bonds will be paid using assessments levied by City Y on the customers of the utility. Although the utility lines are privately owned and the utility customers make payments to the utility company for the use of those lines, the assessments are payments in respect of the cost of relocating the utility line. Thus, the assessment payments are not made in respect of property used for a private business use. Any direct or indirect payments to Y by the utility company for the undergrounding are, however, taken into account as private payments.

Example 5. Payments from users of proceeds that are not private business users taken into account. City P issues general obligation bonds to finance the renovation of a hospital that it owns. The hospital is operated for P by D, a nongovernmental person, under a management contract that results in private business use under § 1.141-3. P will use the revenues from the hospital (after the required payments to D and the payment of operation and maintenance expenses) to pay the debt service on the bonds. The bonds meet the private security or payment test because the revenues from the hospital are payments in respect of property used for a private business use.

Example 6. Limitation of amount of payments to amount of private business use not determined annually. City Q issues bonds with a term of 15 years and uses the proceeds to construct an office building. The debt service

on the bonds is level throughout the 15-year term. Q enters into a 5-year lease with Corporation R under which R is treated as a user of 11 percent of the proceeds. R will make lease payments equal to 20 percent of the annual debt service on the bonds for each year of the lease. The present value of R's lease payments is equal to 12 percent of the present value of the debt service over the entire 15-year term of the bonds. If, however, the lease payments taken into account as private payments were limited to 11 percent of debt service paid in each year of the lease, the present value of these payments would be only 8 percent of the debt service on the bonds over the entire term of the bonds. The bonds meet the private security or payment test, because R's lease payments are taken into account as private payments in an amount not to exceed 11 percent of the debt service of the bonds.

Example 7. Allocation of payments to funds not derived from a borrowing. City Z purchases property for \$1,250,000 using \$1,000,000 of proceeds of its tax increment bonds and \$250,000 of other revenues that are in its redevelopment fund. Within 60 days of the date of purchase, Z declared its intent to sell the property pursuant to a redevelopment plan and to use that amount to reimburse its redevelopment fund. The bonds are secured only by the incremental property taxes attributable to the increase in value of the property from the planned redevelopment of the property. Within 18 months after the issue date, Z sells the financed property to Developer M for \$250,000, which Z uses to reimburse the redevelopment fund. The property that M uses is financed both with the proceeds of the bonds and Z's redevelopment fund. The payments by M are properly allocable to the costs of property financed with the amounts in Z's redevelopment fund. See paragraphs (c)(3) (i) and (v) of this section.

Example 8. Allocation of payments to different sources of funding—improvements. In 1997, City L issues bonds with proceeds of \$8 million to finance the acquisition of a building. In 2002, L spends \$2 million of its general revenues to improve the heating system and roof of the building. At that time, L enters into a 10-year lease with Corporation M for the building providing for annual payments of \$1 million to L. The lease payments are at fair market value, and the lease payments do not otherwise have a significant nexus to either the issue or to the expenditure of general revenues. Eighty percent of each lease payment is allocated to the issue and is taken into account under the private payment test because each lease payment is properly allocated to the sources of funding in a manner that reasonably corresponds to the relative amounts of the sources of funding that are expended on the building.

Example 9. Security not provided by users of proceeds not taken into account. County W

issues certificates of participation in a lease of a building that W owns and covenants to appropriate annual payments for the lease. A portion of each payment is specified as interest. More than 10 percent of the building is used for private business use. None of the proceeds of the obligations are used with respect to the building. W uses the proceeds of the obligations to make a grant to Corporation Y for the construction of a factory that Y will own. Y makes no payments to W, directly or indirectly, for its use of proceeds, and Y has no relationship to the users of the leased building. If W defaults under the lease, the trustee for the holders of the certificates of participation has a limited right of repossession under which the trustee may not foreclose but may lease the property to a new tenant at fair market value. The obligations are secured by an interest in property used for a private business use. However, because the property is not provided by a private business user and is not financed property, the obligations do not meet the private security or payment test.

Example 10. Allocation of payments among issues. University L, a political subdivision, issued three separate series of revenue bonds during 1989, 1991, and 1993 under the same bond resolution. L used the proceeds to construct facilities exclusively for its own use. Bonds issued under the resolution are equally and ratably secured and payable solely from the income derived by L from rates, fees, and charges imposed by L for the use of the facilities. The bonds issued in 1989, 1991, and 1993 are not private activity bonds. In 1997, L issues another series of bonds under the resolution to finance additional facilities. L leases 20 percent of the new facilities for the term of the 1997 bonds to nongovernmental persons who will use the facilities in their trades or businesses. The present value of the lease payments from the nongovernmental users will equal 15 percent of the present value of the debt service on the 1997 bonds. L will commingle all of the revenues from all its bond-financed facilities in its revenue fund. The present value of the portion of the lease payments from nongovernmental lessees of the new facilities allocable to the 1997 bonds under paragraph (d) of this section is less than 10 percent of the present value of the debt service on the 1997 bonds because the bond documents provide that the bonds are equally and ratably secured. Accordingly, the 1997 bonds do not meet the private security test. The 1997 bonds meet the private payment test, however, because the private lease payments for the new facility are properly allocated to those bonds (that is, because none of the proceeds of the prior issues were used for the new facilities). See paragraph (c) of this section.

Example 11. Generally applicable tax. (i) Authority N issues bonds to finance the construction of a stadium. Under a long-term

lease, Corporation X, a professional sports team, will use more than 10 percent of the stadium. X will not, however, make any payments for this private business use. The security for the bonds will be a ticket tax imposed on each person purchasing a ticket for an event at the stadium. The portion of the ticket tax attributable to tickets purchased by persons attending X's events will, on a present value basis, exceed 10 percent of the present value of the debt service on N's bonds. The bonds meet the private security or payment test. The ticket tax is not a generally applicable tax and, to the extent that the tax receipts relate to X's events, the taxes are payments in respect of property used for a private business use.

(ii) The facts are the same as *Example 11(i)*, except that the ticket tax is imposed by N on tickets purchased for events at a number of large entertainment facilities within the N's jurisdiction (for example, other stadiums, arenas, and concert halls), some of which were not financed with tax-exempt bonds. The ticket tax is a generally applicable tax and therefore the revenues from this tax are not payments in respect of property used for a private business use. The receipt of the ticket tax does not cause the bonds to meet the private security or payment test.

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§ 1.141-5 Private loan financing test.

(a) *In general.* Bonds of an issue are private activity bonds if more than the lesser of 5 percent or \$5 million of the proceeds of the issue is to be used (directly or indirectly) to make or finance loans to persons other than governmental persons. Section 1.141-2(d) applies in determining whether the private loan financing test is met. In determining whether the proceeds of an issue are used to make or finance loans, indirect, as well as direct, use of the proceeds is taken into account.

(b) *Measurement of test.* In determining whether the private loan financing test is met, the amount actually loaned to a nongovernmental person is not discounted to reflect the present value of the loan repayments.

(c) *Definition of private loan*—(1) *In general.* Any transaction that is generally characterized as a loan for federal income tax purposes is a loan for purposes of this section. In addition, a loan may arise from the direct lending of bond proceeds or may arise from transactions in which indirect benefits that are the economic equivalent of a